IV. FRANCHISE SIZE, NOT SYSTEM SIZE, IS THE RELEVANT UNIT OF MEASURE TO IDENTIFY AREAS IN WHICH REGULATORY RELIEF MAY BE AVAILABLE.

SCBA agrees that the plain words of the statute make system size irrelevant. The statute provides that the areas eligible for reduced regulatory burdens are those "franchise area[s] in which that operator services 50,000 or fewer subscribers."[46] The only relevant measure of local service area relevant is the franchise.

As a consequence, a system serving multiple franchise areas could have more than 50,000 subscribers and still qualify. Further, a system could qualify in franchise areas with fewer than 50,000 subscribers and not in other franchise areas with more than 50,000 subscribers.

The Commission must measure these subscribers in terms of equivalent basic subscribers, also referred to as equivalent billing units. The standard unit of measure in the cable industry is the equivalent basic subscriber. When reviewing cable industry data, Congress would have examined statistics computed using equivalent basic subscribers. Similarly, the Commission has adopted an equivalent basic subscriber measure to determine company size qualification. To ensure uniformity of information and application under the law, the Commission should allow operators to use the equivalent basic subscriber measure when determining franchise area qualification.

V. DEREGULATION PROCEDURES: THE COMMISSION SHOULD ADOPT STREAMLINED CERTIFICATION PROCEDURES.

The Commission seeks comment on a procedural mechanism through which an operator can obtain a determination of small operator status.[47] Such procedures should result in a prompt decision

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[46] 47 U.S.C. § 543(m)(1).

[47] *NPRM* at ¶ 90.

with a minimum of paperwork, while allowing LFAs and the Commission the ability to verify subscriber and revenue data only when necessary. SCBA proposes below a procedural mechanism tailored to these requirements.

A. Small Systems That Were Basic Only Systems as of December 31, 1994 Are Deregulated.

As a preliminary matter, SCBA supports the Commission's conclusion that deregulation for basic only systems under Section 301(c) "depends solely upon the number of tiers that were subject to regulation as of December 31, 1994."[48] Neither the language of Section 301(c) nor the legislative history support a contrary conclusion. Similarly, there are no sound policy reasons to support application of the "change in the fundamental nature of the tier" test for any additional tiers that were launched after December 31, 1994. The statute aims to provide greater deregulation for small cable and should not be interpreted to exclude companies from deregulation because a NPT was launched or a tier restructuring occurred in 1995. The statute directs a bright line test. If a cable company satisfies the size and affiliation standards and offered only basic service as of December 31, 1994, it is deregulated.

B. Certification Procedures Should Be Streamlined and Include Protection from Unreasonable Information Requests.

1. A Simple Declaration Initiates the Procedure.

SCBA supports the Commission's proposed certification procedures,[49] with modifications. As proposed by the Commission, an operator may submit a certification to an LFA at any time. <u>The</u>

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[48] *Id.*

[49] *Order* at ¶¶ 28-30.

Commission should specify that an operator may submit the certification in the form of a simple declaration.

2. LFAs Must Decide Within 60 Days.

To streamline the procedure, the Commission should reduce the decision time to 60 days from the time of filing of the certification. This will better balance the operator's need for prompt local action and certainty in regulatory status than the proposed 90 days. An even more rapid approach would be to reduce the decision time to 30 days, the same number of days for the Commission to consider an LFA's certification to regulate basic rates. SCBA understands that due to the schedules of many municipal governments, a 30-day window may prove too abbreviated. If an LFA does not render a decision in 60 days, the declaration shall be deemed approved.

3. Protection Against Unreasonable Information Requests.

The Commission should provide procedural protection for cable operators that may be subject to unreasonable information requests by LFAs. As in Form 1230 rate regulation, the Commission should urge LFAs to carefully limit their requests for information.[50] If a cable operator believes that a request by an LFA for additional information to support a deregulation certification is unreasonable, the operator may file an interlocutory appeal with the Commission. The Commission shall act promptly on the appeal and may approve the declaration, rule on the appeal or remand the case to the LFA.

[50] *Small System Order* at ¶ 65.

4. The Procedure Shall Also Apply in Cases Involving Proposed CPST Complaints.

The Commission should specify that the above procedures also apply when an operator files a declaration in response to an LFA's notice that it intends to file a CPST rate complaint. The LFA will have either 60 days to grant the certification, withdraw notice of its complaint, or file its complaint and place the case before the Commission.

C. The Procedures Should Apply to All Certifications of Small Cable Company Status.

SCBA discourages the Commission from establishing distinct procedures for small cable companies that "clearly qualify" and other procedures where qualification questions come closer to the statutory criteria. The combination of a 60 day decision window, a tolling period for legitimate information requests, and an interlocutory appeal route to the Commission will ensure prompt and reasonable decisionmaking. In rare cases where these procedures do not serve a particular LFA or cable operator, they may take the case to the Commission on a petition for special relief. The possibility of such cases should not discourage the Commission from establishing a streamlined means of obtaining deregulated status with a minimum of paperwork.

VI. EFFECTIVE COMPETITION: THE COMMISSION SHOULD RETAIN ITS CURRENT DEFINITION OF "COMPARABLE PROGRAMMING".

SCBA comments on the Commission's proposed definition of "comparable programming" for the new prong of the effective competition test. The interim rules and the proposed rules will create unnecessary burdens on small cable and will be subject to manipulation by competitors. To avoid these consequences, the Commission should retain the existing definition of "comparable programming," with a slight modification.

A. Comparison of Definitions of Comparable Programming.

Section 301(b)(3) of the Act adds a new test for effective competition. A key element of this test is that LEC-delivered programming be "comparable" to that of the cable operator. The Conference Report defines "comparable programming" in this context as "access to at least 12 channels of programming, at least some of which are television broadcasting signals."[51] This definition generally aligns with the current definition of "comparable programming" for the competitive provider prong of the effective competition test:

> In order to offer comparable programming within the meaning of paragraph (b)(2)(i) of this section, a competing multichannel video programming distributor must offer at least 12 channels of video programming, including at least one channel of non-broadcast service programming.[52]

The *Order* adopts an interim rule defining "comparable programming" that differs significantly from the existing definition. For the purpose of the new effective competition test, an MMDS operator owned by or affiliated with a LEC offers comparable programming in two circumstances: (1) if the MMDS provider offers at least one broadcast channel without an A/B switch or comparable device; or (2) if the MMDS provider installs a required A/B switch.[53] The *Order* also implies a set of circumstances where a LEC owned or affiliated MMDS provider *may* offer comparable programming:

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[51]Conference Report at 170.

[52]47 C.F.R. § 76.905(g).

[53]*Order* at ¶ 14.

> Inclusion of broadcast channels on the MMDS operator's rate card, advertising, or other marketing materials may be evidence that the MMDS operator offers the broadcast channels in accordance with our definition of 'offer'.[54]

The *Order* also excludes from the definition of "broadcast channels" any "broadcast programming delivered by satellite (e.g. 'superstations')."[55] The *NPRM* seeks comment on these standards.

B. The Commission Should Not Adopt the Interim Definition.

The Commission should *not* adopt the interim definition of "comparable programming." As recognized in the *NPRM*, "a single definition of 'comparable programming' should apply to both prongs of the effective competition test in which the term is used."[56] <u>The interim rule will impose significantly increased administrative burdens on small cable companies</u>, particularly if it is applied to both effective competition tests. The existing definition with a slight modification remains a more workable standard.

The interim rule will make establishing effective competition problematic in cases involving LEC-affiliated MMDS operators. Application of the definition to all competing providers will substantially exacerbate the problem. Under the interim rule, to establish effective competition, a cable operator must gather evidence concerning how a competitor provides access to broadcast stations. Commission rules provide no authority for cable operators to request such information. Presumably, small cable companies would have to invest in analysis of marketing information, subscriber interviews and other means of gleaning the necessary evidence. Competitors will have the incentive to remain uncooperative so as to make more difficult a cable company's effort to liberate

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[54] *Id.*

[55] *Order* at ¶ 12.

[56] *NPRM at* ¶ 70.

itself from the costs and burdens of regulation. In some cases, LEC-affiliated MMDS operators may attempt to exploit the rules by requiring customers to take some small act that might amount to "installation" of an A/B switch. A cable operator would then bear the burden of showing that the MMDS provider still provided comparable programming, notwithstanding a customer act of "installation."

Universal application of the proposed definition would undermine the effective competition standard. Some delivery vehicles such as DBS do not include a local off-air component. Consequently, the presence of some competitors would never trigger effective competition, keeping cable locked in regulatory shackles, unable to effectively compete.[57]

C. A Slight Modification of the Existing Definition Will Efficiently Effectuate the Act.

Retention of the existing definition, with only slight modification, will help achieve the Commission's goals of adopting clear rules to streamline Commission processes and effectuating the intent of Congress. Under the existing definition, a cable operator can establish comparable programming by a competing provider by producing a rate card showing at least one non-broadcast station. The Commission can amend this definition as follows to maintain this administrative efficiency:

> In order to offer comparable programming within the meaning of this section, a competing multichannel video programming distributor must offer at least 12 channels of video programming, <u>including at least one channel of non-broadcast service programming and one channel of broadcast programming</u>. Reception by a subscriber

[57]For example, the Commission has before it a case of an MMDS provider attempting to stifle a cable operator's ability to meet spot competition by seeking enforcement of uniform pricing rules, despite the operator's assertion that effective competition exists. *Tri-Lakes Cable, Monument, Colorado*, Petition for a Determination of Effective Competition, CSR No. 4724-E ("*Tri-Lakes Cable*").

> of a competing multichannel video programming distributor of at least one channel of broadcast programming and one channel of non-broadcast programming creates a presumption of comparable programming.

This rule will harmonize the existing rule with the indicated intent of Congress in enacting the new effective competition test. This rule will also reduce the administrative burdens and costs on small cable companies that must seek a change in their regulatory status while facing competing providers, LEC-affiliated or otherwise.

VII. CABLE-TELCO BUYOUTS: SMALL CABLE NEEDS SPECIFIC WAIVER PRESUMPTIONS AND PROCEDURES.

Section 302(a) of the Act creates new Communications Act § 652 and establishes restrictions on acquisitions and joint ventures involving LECs and cable operators providing cable service within the LEC's telephone service area. The *Order* incorporates the statutory language into Commission rules.[58] SCBA comments on this action because transactions with LECs represent an important source of capital for small cable. The Commission should interpret Section 302(a) so as to not unnecessarily cut off small cable from such transactions.

A. The Commission Should Specify That the Income Limit in Section 652(d)(5) Does Not Include Affiliate Income.

Section 652(d)(5) creates an exception for certain transactions involving smaller LEC and smaller cable companies.[59] Because many of SCBA's members provide cable service through small

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[58] *Order* at ¶ 44.

[59] It states:

> a local exchange carrier with less than $100,000,000 in annual operating revenues (or any affiliate of such carrier owned by, operated by, controlled by, or under common control with such carrier) may purchase or otherwise acquire more than a 10 percent financial interest in, or any management interest in, or enter into joint venture

systems in generally nonurbanized areas, application of this exception is critical to opening up opportunities to obtain capital from a LEC that does not qualify for the extremely restrictive exception for rural systems in Section 652(d)(1).

The Commission can adopt a standard for application of Section 652(d)(5) specifying that the $100 million annual operating revenue threshold is applied only to the LEC *or* its affiliate that transacts with a qualifying cable company. The Commission should clarify that the $100 million annual operating revenue threshold is not an aggregation of all operating revenue from the LEC and all its affiliates. Both the statutory language and Congressional intent support this.

The plain language of Section 652(d)(5) specifies that the relevant annual operating revenue is that of the LEC. Congress did not specify that affiliates revenues were to be included. If the LEC qualifies, so do its affiliates. This contrasts with Section 301(c)(2) where Congress specified that the $250 million small cable company threshold measured the gross revenues of an affiliate. This reflects Congressional intent to allow non-Tier I LECs to invest in qualifying cable companies in excess of a 10% financial interest.

The Commission will further its objectives of adopting clear rules to streamline its processes and establishing certainty for cable operators by specifying that the annual revenue threshold applies to LEC revenue or the revenue of the affiliate that transacts with the cable company. This will create

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> or partnership with, any cable system within the local exchange carrier's telephone service area that services no more than 20,000 serves no more than 20,000 cable subscribers, if no more than 12,000 of those subscribers live within an urbanized area, as defined by the Bureau of the Census.

certainty for parties that qualify for the exception and facilitate efficient transactions that provide capital for small cable systems serving nonurban areas.

B. The Commission Should Establish Presumptions and Expedited Procedures for Small Cable Company Waivers.

Section 652(d)(6) provides that the Commission may waive the buy-out restrictions in certain circumstances. The waiver provisions are particularly important for small cable companies that do not qualify for the exceptions in Section 652(d)(1) or (5). The Commission should promulgate presumptions and expedited procedures for a waiver process for small cable companies. To require a protracted, fact-intensive proceeding to obtain a waiver will effectively exclude many small cable companies from the waiver process. They cannot afford the administrative burdens and costs of a Commission proceeding.[60] Moreover, LEC investors are less likely to commit to a transaction when consummation will remain subject to the results of a Commission proceeding of unspecified duration.

Consequently, SCBA proposes that the Commission adopt rules that make a waiver a realistic possibility for small cable.

First, the Commission should establish a presumption when a waiver petition is submitted by a small cable company as defined by Section 301(c)(2) of the Act. In such cases, the Commission should presume that "the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served." The record before the Commission shows that small cable companies have a much more difficult time accessing capital and that access to capital is critical for

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[60]See *Small System Order* at ¶55.

upgrading plant and expanding services.[61] No portion of the record suggests any tendency by small cable to engage in anticompetitive conduct that would suggest a need for a prophylactic measure to protect the public interest. To the contrary, the Commission has recognized the public interest in a healthy small cable industry.[62] Facilitating efficient investment in small cable by certain LECs will serve this interest.

Second, the Commission should establish a procedural framework that provides investors and cable operators with certainty. An adaptation of the Form 1230 process provides a model. The Commission should establish a 90-day decision period at both the LFA and Commission levels. If a waiver petition is not acted upon during this period, it should be deemed approved. To assist in the protection of subscribers' interests, LFAs or the Commission could toll this period with a bona fide request for additional information. Small cable companies should have the procedural option of the interlocutory appeal of an LFA information request to the Commission.

With these rules in place, small cable companies will have additional access to sources of capital from LECs in cases where any evidence of the anticompetitive effects of the transaction are negligible.

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[61]See *Small System Order* at ¶28.

[62]See generally, *Small System Order*.

VIII. TECHNICAL REQUIREMENTS: COMMISSION REGULATIONS SHOULD CLARIFY THAT LFAs CAN NO LONGER MANDATE SPECIFIC SYSTEM TECHNOLOGY.

Section 301(e) of the Act preempts state and LFA authority over a cable system's use of any type of subscriber equipment or transmission technology.[63] This represents a significant step toward allowing market forces and customer preference to determine system technology, rather than local regulators. The Commission seeks comment on how Section 301(e) affects the cable franchising, renewal or transfer process.[64]

A. The Commission Can Readily Reconcile Section 301(e) with Other Provisions of the Communications Act.

The Commission can reconcile Section 301(e) and other provisions of the Communications Act in ways that maximize market forces and minimize the distorting effects of regulatory interference. <u>Particularly for small cable companies, LFA specified subscriber equipment and plant technology impose substantial burdens on an operator's ability to respond to consumer preference and competition</u>. Many SCBA members have faced franchise renewal negotiations where an LFA conditions a grant of renewal on extremely specific technical upgrades of system plant and electronics, often based on a municipal consultant's opinion as to the "state of the art" to which the municipality is "entitled." Similarly, many LFAs impose requirements that if a cable operator upgrades technology in a neighboring system, it must do the same in the system regulated by the LFA. <u>These types of mandated technological upgrades skew efficient allocation of resources</u>. They either

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[63]Section 301(e) replaces the last two sentences of 47 U.S.C. § 544(e) with "No state or franchising authority may prohibit, condition, or restrict a cable system's use of any type of subscriber equipment of any transmission technology."

[64]*NPRM* at ¶ 104.

create disincentives to upgrade or result in upgrades for which subscribers do not care to pay. In either case, a small cable company's ability to compete is impaired.

B. Reconciling Franchise Renewal and Grant Provisions.

Consequently, the Commission can reconcile Section 301(e) with the renewal and transfer provisions as follows:

- Under 47 U.S.C. § 546(c)(1)(B), as part of formal renewal proceedings, an LFA can consider the quality of an operator's service, including signal quality. The Commission should find that under Section 301(e), an LFA *cannot* consider the operator's selection of subscriber equipment and transmission technology. As a practical matter, most small cable companies upgrade bandwidth, electronics and plant as capital to do so becomes available and customers appear willing to pay for such upgrades. Allowing local regulators to second guess selection of equipment and transmission technology during franchise renewal interferes with market determination of efficient investments in equipment and plant.
- Under 47 U.S.C. § 546(c)(1)(C), as part of formal renewal proceedings, an LFA can consider an operator's technical ability insofar as it relates to an operator's proposal. For example, an LFA might consider if a cable company has adequately trained personnel to install, operate and service equipment and transmission technology specified *by the operator*. Under Section 301(e), the Commission should find that an LFA cannot use "consideration of technical

ability" as a means to require specified subscriber equipment and transmission technology.

- Under 47 U.S.C. § 546(b)(2), an LFA may require submission by an operator of a renewal proposal that includes "proposals for an upgrade of the cable system." The Commission can also readily reconcile this section with Section 301(e). Section 546(b)(2) is expressly subject to section 544, which now prohibits an LFA from requiring use of any type of subscriber equipment or transmission technology. Insofar as an LFA mandated renewal proposal requires upgrades in such equipment, it is preempted by Section 544. LFAs may still seek proposals that include system upgrades, but such proposals cannot require specific equipment and transmission technology including required bandwidth. Investments in such capital intensive assets should be market-driven, not regulator driven.

The same interpretations can apply to the provisions of 47 U.S.C. § 541(a)(4) regarding an LFA requiring "adequate assurance that the cable operator has the [technical] qualifications to provide cable service."

By clarifying these interpretive issues in this way, the Commission can effectuate the intent of Congress and provide small cable and investors with certainty. The Commission can make clear that local regulators cannot demand inefficient allocation of resources in customer equipment and transmission technology.

IX. OTHER MATTERS: DEREGULATED SMALL CABLE COMPANIES SHOULD NOT BE SUBJECT TO THE UNIFORM RATE REQUIREMENT.

The Commission seeks comment on proposals to ease the burdens of regulation.[65] SCBA requests that the Commission consider one proposal that will fully implement Congress' intent to remove the burdens of rate regulation from many small cable systems. In conjunction with the rules implementing the small cable company provisions of the Act, SCBA proposes that the Commission remove the uniform rate requirement from deregulated small cable companies.

Removing the uniform rate requirement from deregulated small cable companies will be fully consistent with the Act, Congressional intent and the Commission's goal of streamlining regulation. The Act codifies the result of *Time Warner Entertainment Co. v. FCC* and removes the uniform rate requirement from systems that are deregulated due to effective competition.[66] As stated in the *Order*, since the 1992 Cable Act:

> regulation of cable television has been guided by Congress's intent to 'rely on the marketplace, to the maximum extent feasible . . .' The 1992 Cable Act required the Commission to prescribe rate regulations that protect subscribers from having to pay unreasonable rates by ensuring that rates for regulated services do not exceed rates that would be charged in the presence of effective competition. . . Where effective competition is present, certain other regulatory requirements also become inapplicable, including the uniform rate requirement . . .[67]

Section 301(c) of the Act shows that Congress concluded that certain small systems shall no longer remain subject to rate regulation. Because Congress has obviated the need for LFA or Commission

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[65] *NPRM* at ¶ 112.

[66] 56 F.3d 151, 189 (D.C. Cir. 1995).

[67] *Order* at ¶ 5.

rate regulation for these systems, any need to maintain the uniform rate requirement also becomes questionable.

As shown by at least one case currently before the Commission involving a small cable company, MVPDs are now using the uniform rate requirement to attack small cable competitions.[68] In *Tri-Lakes Cable*, American Telecasting, Inc., the nation's largest MMDS company, is attempting to use the uniform rate requirement to threaten and harass a small cable competitor that offers promotional and introductory discounts. After escalating threats from ATI, Tri-Lakes had little choice but to invest in the filing of a petition for determination of effective competition. This represents a substantial investment for a cable company serving a franchise area of 372 occupied households![69] The Commission could remove this anticompetitive weapon against small cable competitors by finding that small systems that are completely rate deregulated are no longer subject to the uniform rate requirement.

SCBA believes there is no information before the Commission that suggests any conduct by small cable companies eligible for deregulation warranting imposing the uniform rate requirement on such companies. Removal of the requirement for such companies will reduce unnecessary regulation and permit small cable to more efficiently compete.

X. CONCLUSION

As indicated in these Comments, the Commission can implement the Act in a manner that provides meaningful relief to small cable. SCBA has outlined the pitfalls the Commission should avoid and has provided concrete suggestions for substantive and procedural regulations. SCBA

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[68] *Tri-Lakes Cable*, supra.

[69] 1990 Census data.

remains ready to provide the Commission with any additional information to assist in the proper implementation of the Act's small cable provisions.

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EXHIBIT A

opment (AA/MSB&COD) or his or her designee (See § 124.102(b)).

(4) Formal size determinations (§§ 121.1601 through 121.1608 of this part) pursuant to a request therefore by an applicant for any assistance program of SBA not otherwise provided for, adversely affected by a size status finding made by an official of SBA, or by a size status finding made by a participating financial institution or a small business investment company in connection with an application for financial assistance §§ 121.801 through 121.806. Formal size determinations shall also be made by the Regional Office in connection with applications for program assistance upon request by the appropriate program official of SBA, a participating financial institution or a small business investment company.

(b) Except for SBA's small business set-aside program and SBA's Small Business Innovation Research program, formal size determinations shall be made by the SBA Regional Office serving the geographical area in which the principal office of the protested concern or applicant concern, excluding its affiliates, is located. Formal size determinations in the small business set-aside program and SBA's Small Business Innovation Research program shall be made by the SBA Regional Office serving the geographical area of the headquarters of the offeror, regardless of the location of parent companies or affiliates.

(c) The Regional Administrator may request a formal size determination whenever he/she deems it appropriate.

DEFINITIONS

§ 121.401 Affiliation.

(a) *General rule.* (1) Except as otherwise noted, size determinations shall include the applicant concern and all its domestic and foreign affiliates. Moreover, all affiliates, regardless of whether organized for profit, must be included.

(2) Except as otherwise provided in this section, concerns are affiliates of each other when either directly or indirectly

(i) One concern controls or has the power to control the other, or

(ii) A third party or parties controls or has the power to control both, or

(iii) An *identity of interest* between or among parties exists such that affiliation may be found.

(3) In determining whether affiliation exists, consideration shall be given to all appropriate factors, including common ownership, common management, and contractual relationships.

(b) *Exclusion from affiliation coverage.* Portfolio or client concerns owned in whole or substantial part by investment companies licensed, or development companies qualifying under the Small Business Investment Act of 1958, as amended, or by Investment Companies registered under the Investment Company Act of 1940, as amended, concerns owned and controlled by Indian Tribes, or concerns owned and controlled by Alaska Regional or Village Corporations organized pursuant to the Alaska Native Claims Settlement Act (43 U.S.C. 1601, *et seq.*) are not considered affiliates of such investment companies, development companies, tribes or Alaska Regional or Village Corporations.

(c) *Nature of control in determining affiliation.* (1) Every business concern is considered to have one or more parties who directly or indirectly control or have the power to control it. Control may be affirmative or negative and it is immaterial whether it is exercised so long as the power to control exists.

Example. A party owning 50 percent of the voting stock of a concern would have negative power to control such concern since such party can block any action of the other stockholders. Also, the bylaws of a corporation may permit a stockholder with less than 50 percent of the voting stock to block any actions taken by the other stockholders. Affiliation exists when one or more parties have the power to control a concern while at the same time another party, or other parties, may be in control of the concern at the will of the party with the power to control.

(2) Control can arise through stock ownership; occupancy of director, officer or key employee positions; contractual or other business relations; or combinations of these and other factors.

(3) Control can arise through management positions where a concern's voting stock is so widely distributed

that no effective control can be established.

Example. In a corporation where the officers and directors own various size blocks of stock totaling 40 percent of a concern's voting stock, but no officer or director has a block sufficient to give him control or the power to control and the remaining 60 percent is widely distributed with no individual stockholder having a stock interest greater than 10 percent, management has the power to control.

(d) *Identity of interest between and among persons as an affiliation determinant.* Affiliation can arise between or among two or more persons with an identity of interest, such as members of the same family or persons with common investments in more than one concern. In determining who controls or has the power to control a concern, persons with an identity of interest may be treated as though they were one person.

(e) *Affiliation through stock ownership.*(1) A person is presumed to control or have the power to control a concern if he or she owns or controls or has the power to control 50 percent or more of its voting stock.

(2) A person is presumed to control or have the power to control a concern even though he or she owns, controls or has the power to control less than 50 percent of the concern's voting stock, if the block of stock he or she owns, controls or has the power to control is large as compared with any other outstanding block of stock.

(3) If two or more persons each owns, controls or has the power to control less than 50% of the voting stock of a concern, such minority holdings are equal or approximately equal in size, and the aggregate of these minority holdings is large as compared with any other stock holding, the presumption arises that each such person individually controls or has the power to control the concern; however, such presumption may be rebutted by a showing that such control or power to control, in fact, does not exist.

EXAMPLE: Assume that Firms A and B each own 40 percent of Firm C. Assume further that Firm A has 200 employees, Firm B has 400 employees, Firm C alone has 50 employees and that the applicable size standard is 500 employees. This subsection requires that both Firm A and Firm B be considered to individually control Firm C and that their employees be aggregated with those of Firm C to determine Firm C's size. Therefore, Firm C would be considered other than small because Firm A's employees plus its employees plus Firm B's employees (200 + 50 + 400) would exceed the 500 employee size standard.

(f) *Affiliation arising under stock options, convertible debentures, and agreements to merge.* Stock options, convertible debentures, and agreements to merge (including agreements in principle) are generally considered to have a present effect on the power to control the concern. Therefore, in making a size determination, such options, debentures, and agreements are generally treated as though the rights held thereunder had been exercised. However, an affiliate cannot use such options and debentures to appear to terminate its control over another concern before it actually does so.

EXAMPLE 1. If company "A" holds an option to purchase a controlling interest in company "B," the situation is treated as though company "A" had exercised its rights and had become owner of a controlling interest in company "B." The employees or annual receipts, as the case may be, of both concerns must be taken into account in determining size.

EXAMPLE 2. If large company "A" holds 70% (70 of 100 outstanding shares) of the voting stock of company "B" and gives a third party an option to purchase 50 of the 70 owned by "A" shares of concern "B", company "B" will be deemed to be an affiliate of company "A" until the third party actually exercises its option to purchase such shares. In order to prevent large company "A" from circumventing the intent of the regulation which sells present effect to stock options, the option is not considered to have present effect in this case.

EXAMPLE 3. If company "A" has entered into an agreement to merge with company "B" in the future, the situation is treated as though the merger has taken place.

(g) *Affiliation under voting trusts.* (1) If the primary purpose of a voting trust, or similar agreement, is to separate voting power from beneficial ownership of voting stock for the purpose of shifting control of or the power to control a concern in order that such concern or another concern may qualify as a small business within the size regulations, such voting trust shall not be considered valid for this purpose regardless of whether it is or is not recognized within the appropriate jurisdiction. However, if a voting trust is primarily entered into for a legitimate purpose other than that described above, and it is recognized within the appropriate jurisdiction, it may be considered valid for the purpose of a size determination.

(2) Agreements to divest (including agreements in principle) are not considered to have a present effect on the power to control the concern.

(h) *Affiliation through common management*. Affiliation generally arises where officers, directors, or key employees serve as the majority or otherwise as the controlling element of the board of directors and/or the management of another concern.

(i) *Affiliation through common facilities*. Affiliation generally arises where one concern shares office space and/or employees and/or other facilities with another concern, particularly where such concerns are in the same or related industry or field of operations, or where such concerns were formerly affiliated.

(j) *Affiliation with a newly organized concern*. Affiliation generally arises where former officers, directors, principal stockholders, and/or key employees of one concern organize a new concern in the same or a related industry or field of operation, and serve as its officers, directors, principal stockholders, and/or key employees, and the one concern is furnishing or will furnish the other concern with subcontracts, financial or technical assistance, bid or performance bond indemnification, and/or other facilities, whether for a fee or otherwise.

(k) *Affiliation through contractual relationships*. Affiliation generally arises where once concern is dependent upon another concern for contracts and business to such a degree that its economic viability would be in jeopardy without such contracts/business.

(l) *Affiliation under joint venture arrangements*. (1) A joint venture for size determination purposes is an association of concerns and/or individuals, with interests in any degree or proportion, formed by contract, express or implied, to engage in and carry out a single, specific business venture for joint profit for which purpose they combine their efforts, property, money, skill and knowledge, but not on a continuing or permanent basis for conducting business generally. The determination whether an entity is a joint venture is based upon the facts of the business operation, regardless of how the business operation may be designated by the parties involved. An agreement to share profits/losses proportionate to each party's contribution to the business operation is a significant factor in determining whether the business operation is a joint venture.

(2) For the purpose of financial assistance to a joint venture, the parties thereto are considered to be affiliated with each other. Where the financial assistance, however, is to a concern for its own use, outside the joint venture, an affiliation determination shall not automatically arise from the existence of the joint venture arrangement. In this latter situation, the existence of affiliation shall be determined under these regulations.

(3) Concerns bidding on a particular procurement or property sale as joint venturers are affiliated with each other with regard to performance of the contract. This determination of affiliation does not extend to other contracts or business outside the joint venture arrangement.

(4) An ostensible subcontractor which performs or is to perform primary or vital requirements of a contract may have such a controlling role that it must be considered a joint venturer affiliated on the contract with the prime contractor. In determining whether subcontracting rises to the level of affiliation as a joint venture, SBA considers whether the prime contractor has unusual reliance on the subcontractor.

(5) Even though a concern might not be an affiliate of its joint venturers for the purpose of operations apart from the joint venture, it nevertheless must include its proportionate share of the joint venture receipts or employees in determining its eligibility under the size standards.

(m) *Affiliation under franchise and license agreements*. In determining whether the franchisor controls or has the power to control and, therefore, is affiliated with the franchisee, the restraints, relating to standardized quality, advertising, accounting format and other provisions, imposed on a franchisee by its franchise agreement shall generally not be considered, provided that the franchisee has the right to profit from its efforts and bears the risk of loss commensurate with ownership. Alternatively, even though a franchisee may not be controlled by the franchisor by virtue of such provisions in the franchise agreement, control and, thus, affiliation could arise through other means, such as common ownership, common management or excessive restrictions upon the sale of the franchise interest.

[54 FR 52643, Dec. 21, 1989, as amended at 55 FR 27199, July 2, 1990]

§ 121.402 Annual receipts.

(a) In size determinations where the standard is *annual receipts*, size eligibility requires that the concern may not exceed the *annual receipts* in that standard.

(b) *Definitions*. For the purpose of determining annual receipts of a concern:

(1) *Accrual basis* means a method of accounting in which accounts and notes receivable are recorded in the regular books of account for the period in which the firm first has a claim of right to them. *Claim of right* has the meaning attributed to it by the U.S. Internal Revenue Service (IRS).

(2) *Receipts* is defined to include all revenue in whatever form received or accrued from whatever source, including from the sales of products or services, interest, dividends, rents, royalties, fees, or commissions, reduced by returns and allowances. However, the term *receipts* excludes proceeds from sales of capital assets and investments, proceeds from transactions between a concern and its domestic and foreign affiliates, amounts collected for another by a travel agent or real estate agent, and taxes collected for remittance to a taxing authority.

(3) *Regular books of account* means the general ledger or other book of final entry and, if used, the journals or other books of original entry.

(4) *Completed fiscal year* means a taxable year including any short period. *Taxable year* and *short period* have the meaning attributed to them by the IRS.

(5) Unless otherwise defined in this section, all terms shall have the meaning attributed to them by the IRS.

(c) *Period of measurement. Annual Receipts* of a concern which has been in business for 3 or more completed fiscal years means the arithmetic annual average revenue of the concern over its last 3 completed fiscal years (total revenue compiled over the entire 3-year period would be divided by three). *Annual Receipts* of a concern which has been in business for less than 3 fiscal years means the arithmetic annual average revenue over the time period the concern has been in business. (Total revenues compiled over the period the concern has been in business, divided by the number of weeks, including fractions of a week, the concern has been in business, multiplied by 52). *Annual receipts* of a concern which has been in business three or more years but has a short year in the last three years will be the arithmetic annual average revenue over the two full years and the short year. See paragraph (d)(3) of this section. The short period may appear at the beginning, middle or end of the three year calculation period.

(d)(1) *Method of determining annual receipts*. Revenue may be taken from the regular books of account of the concern. If the concern so elects, or has not kept regular books of account, or the IRS has found such records to be inadequate and has reconstructed income of the concern, then revenues shown on the Federal Income Tax return of the concern may be used in determining annual receipts. Subject to the exception in paragraph (d)(2) of this section, revenue shown on the regular books of account or the Federal Income Tax return on a basis other than accrual must be restated to show revenue on an accrual basis for all fiscal years beginning on or after January 1, 1990. For purposes of either a self-certification as to size made, or any size determination initiated or completed, subsequent to January 22, 1992, a firm may elect to show revenues for fiscal years beginning *prior to* January 1, 1990, on either a cash or an accrual basis of accounting. Further, where the completed contract method of determining income has been used, revenue must be restated to a percentage of completion

Exhibit D

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OFFICE OF SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Cable Act Reform Provisions of the Telecommunications Act of 1996	)	CS Docket No. 96-85
	)	
	)	

REPLY COMMENTS OF THE SMALL CABLE BUSINESS ASSOCIATION

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